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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

verizon

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August 31, 2000

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, S.W.
TW-A325-12th Street Lobby
Washington, D.C. 20554

<u>EX PARTE</u>
CC Docket No. 98-137, "In the Matter of 1998 Biennial Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers"

Dear Ms. Salas:

Today, Mr. Frank Gumper, representing Verizon, met with Ms.Dorothy Attwood, Mr. Jack Zinman,. Mr. Jared Carlson, Ms. Carol Mattey and Mr. Tim Peterson to discuss the above referenced proceeding. The discussion reflected the positions that Verizon provided in their written comments and previous Ex Partes already on the public record. A copy of the handout used to guide the discussion is attached.

An original and one copy of this Ex Parte are being filed in the Office of the Secretary today, August 31, 2000. Please include it in the public record of the above referenced proceeding as required under Section 1.1206(b)(2) of the Commission's rules.

Sincerely,

Gerald Asch

Attachment
cc: Ms. Attwood
Mr. Zinman
Mr. Carlson
Ms. Mattey
Mr. Peterson

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List A B C D E

Implementation of Increased Federal Depreciation Will Not Impact Reported State Earnings

While the mechanics of how federal and state depreciation requirements are implemented will vary from carrier to carrier, the distinction between federal and state depreciation requirements is common to all regulated local exchange carriers. Adjustments in federal depreciation policies have no impact on state depreciation. Verizon's former Bell Atlantic carriers provide an example of how these requirements would be implemented. The former Bell Atlantic carriers maintain three sets of financial books: one for financial reporting purposes, one to reflect federal regulation, and one reflecting regulation of the local state regulator.

Depreciation expense is computed each month by multiplying the average investment for the month by 1/12 of the annual depreciation rate for the type of plant in question. The resulting accrual is reported as depreciation expense and credited to the depreciation reserve for the plant account in question. The other entries to the depreciation reserve are retirements, salvage and cost of removal.

Because each set of books has its own depreciation rate, there are actually separate depreciation rates applied to each set of books. The average investment to be depreciated is typically identical or almost identical for Financial, FCC and State. In most cases, however, the prescribed or approved State and FCC depreciation rates are different for the same plant. For that reason we maintain three separate depreciation reserves reflecting the accumulated historic difference in accruals, amortizations or other items impacting the reserves. For the FCC and State books, these reflect the different regulatory decisions that have been made over time. If the FCC were to amortize the difference between current FCC mandated lives and those used for financial reporting, that amortization would be reflected in the reserves on the FCC books, but would have no impact on the State books.

While both the states and the FCC use the same Part 36 separations factors to divide costs, they do not apply those factors to the same base. In particular, depreciation expense is subject to the 75/25 split. But on the State books the 75% factor is applied to a total depreciation expense based on State depreciation rules. On the FCC books, the 25% factor is applied to a depreciation expense calculated using FCC depreciation guidelines. While this means that in any given year the totals will not match 100% of either set of books, over time, all plant is depreciated fully.

For reporting state earnings, intrastate separations factors are applied to State accruals. For federal reporting, the interstate factors are applied to interstate accruals. In the rare case where the State and FCC depreciation rates and reserves are and have been identical, both sets of books are identical and the two separate pieces will add back to total FCC books. Applying the intrastate separations factor to the FCC accruals in most cases, however yields a meaningless number. The separate state record must be, and is, used. As a result, changes in FCC depreciation policy will have no effect on the rate base we use for intrastate regulatory proceedings, the intrastate depreciation expense or the resulting intrastate earnings results.

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